FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

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(Mark One)

[X] Quarterly Report under Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended: September 30, 1994

OR

[ ] Transition report pursuant to section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from __________ to

Commission File Number:
0-19836

America Online, Inc.
(Exact name of registrant as specified in its charter)

Delaware	54-1322110
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

8619 Westwood Center Drive, Vienna, Virginia 22182-2285
(Address of principal executive offices and zip code)

Registrant's telephone number, including area code: (703) 448-8700

Former name, former address, and former year, if changed since last report: Not applicable

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ___X___ No

Indicate the number of shares outstanding of each of the Issuer's classes of Common Stock, as of the latest practicable date.

Title of each class
Common stock $.01 par value
Shares outstanding on October 31, 1994..........7,720,320

AMERICA ONLINE, INC.

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AMERICA ONLINE, INC. AND SUBSIDIARY

CONSOLIDATED BALANCE SHEETS

(Amounts in thousands except share data)

	September 30, 1994 (Unaudited)	June 30, 1994 (Unaudited)
ASSETS		
Current assets:		
Cash and cash equivalents	$ 33,254	$ 43,891
Short-term investments	33,953	24,052
Trade accounts receivable	9,492	8,547
Receivables from affiliate	2,681	1,466
Other receivables	980	570
Prepaid expenses and other current assets	7,542	5,753
Deferred subscriber acquisition costs	29,265	25,459
Total current assets	117,167	109,738
Property and equipment at cost, net	22,339	20,306
Other assets:		
Product development costs, net	9,110	7,912
Deferred subscriber acquisition costs	958	933
License rights, net	141	53
Other assets	2,823	2,800
Deferred income taxes	14,754	12,842
	$ 167,292	$ 154,584
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Trade accounts payable	$ 28,370	$ 15,642
Accrued personnel costs	1,408	896
Other accrued expenses and liabilities	8,115	13,076
Deferred revenue	5,568	4,488
Deferred income taxes	10,977	9,610
Notes payable	253	253
Revolving line of credit	-	1,690
Current portion of long-term debt and capital lease obligations	267	344
Total current liabilities	54,958	45,999
Long-term liabilities:		
Notes payable	5,772	5,836
Capital lease obligations	1,126	1,179
Deferred income taxes	3,777	3,232
Deferred rent	38	41
Total liabilities	65,671	56,287
Stockholders' equity:		
Preferred stock, $.01 par value; 5,000,000 shares authorized, none issued	-	-
Common stock, $.01 par value, 20,000,000 shares authorized, 7,706,635 and 7,692,803 shares issued and outstanding at September 30, 1994 and June 30, 1994, respectively	77	77
Additional paid-in capital	101,125	99,067
Retained earnings (accumulated deficit)	419	(847)
Total stockholders' equity	101,621	98,297
	$ 167,292	$ 154,584

See accompanying notes.

AMERICA ONLINE, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF INCOME

(Amounts in thousands except per share data)

	Three months ended September 30, 1994	Three months ended September 30, 1993
	(unaudited)	
Revenues:		
Online service revenues	$ 50,056	$ 14,299
Marketing service revenues	3,640	3,124
Other revenues	727	1,656
Total revenues	54,423	19,079
Costs and expenses:		
Cost of revenues	31,955	11,165
Marketing	11,295	3,719
Product development	1,757	1,040
General and administrative	5,280	2,624
Total costs and expenses	50,287	18,548
Income from operations	4,136	531
Other income	688	404
Merger expenses	(1,710)	-
Income before provision for income taxes	3,114	935
Provision for income taxes	(1,848)	(632)
Net income	$ 1,266	$ 303
Earnings per share:		
Primary	$ .14	$ .04
Fully diluted	$ .14	$ .04
Weighted average shares outstanding:		
Primary	9,251	7,564
Fully diluted	9,269	7,709

See accompanying notes.

AMERICA ONLINE, INC. AND SUBSIDIARY

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Amounts in thousands)

	Three months ended September 30, 1994	Three months ended September 30, 1993
	(unaudited)	
Cash flows from operating activities:		
Net income	$ 1,266	$ 303
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	1,228	608
Accrued interest	-	30
Amortization of subscriber acquisition costs	9,616	2,629
Loss on sale of property and equipment	37	-
Changes in assets and liabilities:		
Trade accounts receivable	(945)	(412)
Receivables from affiliate	(1,215)	(1,093)
Other receivables	(410)	(89)
Prepaid expenses and other current assets	(1,789)	(1,163)
Other assets	(23)	7
Trade accounts payable	12,728	1,947
Accrued personnel costs	512	153
Other accrued expenses and liabilities	(4,961)	1,998
Deferred revenue	1,080	115
Deferred income taxes	1,848	632
Deferred rent	(3)	(62)
Total adjustments	17,703	5,300
Net cash provided by operating activities	18,969	5,603
Cash flows from investing activities:		
Short-term investments	(9,901)	267
Purchase of property and equipment	(3,175)	(8,487)
Product development costs	(1,589)	(756)
Sale of property and equipment	180	-
Subscriber acquisition costs	(13,447)	(4,907)
Net cash used in investing activities	(27,932)	(13,883)
Cash flows from financing activities:		
Proceeds from issuance of common stock, net	210	255
Proceeds from note payable	-	6,320
Proceeds from issuance of convertible subordinated debt	-	1,000
Principal payments under capital lease obligations	(82)	(48)
Net proceeds (payments) on revolving line of credit	(1,690)	316
Principal and accrued interest payments on notes payable	(112)	(101)
Net cash provided by (used in) financing activities	(1,674)	7,742
Net decrease in cash and cash equivalents	(10,637)	(538)
Cash and cash equivalents at beginning of period	43,891	15,001
Cash and cash equivalents at end of period	$ 33,254	$ 14,463

Supplemental cash flow information		
Cash paid during the period for:		
Interest	138	130
Income taxes	-	-

See accompanying notes.

AMERICA ONLINE, INC. AND SUBSIDIARY

NOTES TO FINANCIAL STATEMENTS

Note 1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements, which include the accounts of America Online, Inc. and its wholly-owned subsidiary, Redgate Communications Corporation, have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring accruals, considered necessary for a fair presentation, have been included in the accompanying unaudited financial statements. All significant intercompany transactions and balances have been eliminated in consolidation. Operating results for the three-month period ended September 30, 1994, are not necessarily indicative of the results that may be expected for the full year ending June 30, 1995. For further information, refer to the financial statements and notes thereto, included in the Company's Annual Report on Form 10-K for the fiscal year ended June 30, 1994.

Note 2. Agreement with Apple Computer

In December 1992 the Company entered into a seven year licensing and development agreement (with renewal provisions to extend the agreement through November 30, 2004) with Apple. Under the agreement, the Company granted Apple a non-exclusive license to use the America Online services platform to provide Apple-branded online services, and has agreed to provide development services to Apple on a fee for services basis. The Company will receive a royalty based on usage, with a total minimum royalty of $15 million over a five year period following the commercial launch of the Apple-branded online service. In addition to royalties, the Company received development funding leading up to the commercial launch of the Apple-branded online service. Apple commercially launched its branded online service, called eWorld, in June 1994. A total of approximately $4.6 million in development funding has been recognized to date under the Apple agreement. A total of $85,000 of development funding and $560,000 of royalty revenue has been recognized as "other revenues" in the three-month period ended September 30, 1994.

As part of the agreement, the Company issued warrants to Apple to purchase 500,000 shares of America Online common stock at an exercise price of $25.00 per share. The warrants are exercisable during the term of the agreement. Under certain circumstances related to a change in control of the Company, the Company can be obligated to purchase the warrants.

Note 3. Agreement with Sprint

In April 1993 the Company entered into an agreement, having a term ending March 31, 1999, with Sprint which provides the Company with more favorable pricing, effective as of January 1, 1993, for use of the Sprint network. Under the agreement, Sprint received a warrant, exercisable during the term of the agreement and subject to certain performance standards specified in the agreement, to purchase 450,000 shares of America Online common stock at a price of $31.25 per share.

Note 4. Income Taxes

The components of the provision for income taxes is as follows:

		Quarter Ended 9/30/94
Current:		
Federal	$	0
State		0
Total	$	0
Deferred		
Federal	$	1,653,000
State		195,000
Total	$	1,848,000
Total	$	1,848,000

The provision for income taxes differs from the amount computed by applying the statutory federal income tax rate to income before provision for income taxes. The sources and tax effects of the differences for the three months ended September 30, 1994 are as follows:

		Amount	Percent
Tax at U.S. statutory rates	$	1,060,000	34.0%
State income taxes, net of related federal benefit		125,000	4.0%
Nondeductible merger expenses		654,000	21.0%
Other		9,000	0.3%
Total	$	1,848,000	59.3%

Deferred income taxes arise because of differences in the treatment of income and expense items for financial reporting and income tax purposes, primarily relating to subscriber acquisition and product development costs.

As of September 30, 1994, the Company had available net operating loss carryforwards of approximately $54,100,000 for tax purposes, which will be available, subject to certain annual limitations, to offset future taxable income. If not used, these loss carryforwards will expire between 2002 and 2010. The Company's net operating loss carryforward includes cumulative deductions of $24,790,000 relating to stockholders' equity (primarily as a result of the exercise of stock options). To the extent that net operating loss carryforwards, when realized, relate to these deductions, the resulting benefits will be credited to stockholders' equity.

Significant components of the Company's deferred tax liabilities and assets as of September 30, 1994 are as follows:

Deferred tax liabilities:	
Capitalized software costs	$ 3,417,000
Deferred subscriber acquisition costs	11,337,000
Net deferred tax liabilities	$ 14,754,000
Deferred tax assets:	
Net operating loss carryforwards	$ 17,730,000
Total deferred tax assets	17,730,000
Valuation allowance for deferred assets	(2,976,000)
Net deferred tax assets	$ 14,754,000

Note 7. Business Combination and Merger Expense

Business Combination

On August 19, 1994, Redgate Communications Corporation ("RCC") was merged with and into a subsidiary of America Online, Inc. ("AOL") and 447,325 shares of AOL's common stock was issued in exchange for all of the outstanding common and preferred stock and warrants of RCC. Additionally, 100,287 shares of AOL's common stock was reserved for outstanding stock options issued by RCC and being assumed by AOL. The merger was accounted for as a pooling of interests, and accordingly, the accompanying financial statements have been restated to include the accounts and operations of RCC for all periods presented prior to the merger.

Separate results of the combining entities for the three months ended September 30, 1994 and 1993 are as follows (amounts in thousands):

	Three Months Ended	
	Sept. 30, 1994	Sept. 30, 1993
Total revenues:		
AOL	$ 50,783	$ 15,955
RCC	3,813	3,124
Less intercompany sales	(173)	-
	$ 54,423	$ 19,079
Net income:		
AOL	$ 3,018	$ 1,029
RCC	(42)	(726)
Merger expenses	(1,710)	-
	$ 1,266	$ 303

Merger Expenses

In connection with the merger of AOL and RCC, $1,710,000 of merger expenses were recognized and have been charged to merger expenses during the three month period ended September 30, 1994. These nonrecurring expenses include investment banking fees, legal and accounting fees, and other miscellaneous expenses.

Note 8. Subsequent Events

In October 1994, the Board of Directors approved a two-for-one stock split of the Company's common stock, effected in the form of a stock dividend of one share for each share outstanding. The stock dividend is payable on November 25, 1994 to stockholders of record at the close of business on November 10, 1994.

In November 1994 the Company entered into agreements to acquire Booklink Technologies, a wholly owned subsidiary of CMG Information Services, and Navisoft, Inc. CMG Information Services will receive $30 million in shares of AOL common stock for all outstanding shares of Booklink Technologies common stock. The number of shares of AOL common stock to be issued will be based on the average closing price of AOL shares for the ten days preceding the closing date. Additionally, AOL common stock will be reserved for outstanding employee options issued by Booklink Technologies. The acquisition of Bookling Technologies is expected to be completed by December 31, 1994, subject to regulatory approval and other customary conditions to closing. Navisoft, Inc. shareholders will receive 65,000 shares of AOL common stock for all outstanding Navisoft common stock, preferred stock, options and warrants. The acquisition of Navisoft, Inc. is expected to be completed by November 30, 1994, subject to customary conditions to closing. Both transactions will be accounted for as a purchase, and will be effected on a tax-free basis.

Item 2. Management's Discussion and Analysis Of Financial Condition and Results of Operations

The following information should be read in conjunction with the consolidated condensed financial statements and the notes thereto included in Item 1 of this Quarterly Report, and the financial statements and the notes thereto and Management's Discussion and Analysis of Financial Condition and Results of Operations contained in the Company's Annual Report on Form 10-K for the year ended June 30, 1994.

The Company's online service revenues are generated primarily from subscribers paying a monthly membership fee and hourly charges based on usage in excess of the number of hours of usage provided as part of the monthly fee. Currently, the Company's standard monthly membership fee, which includes five hours of service, is $9.95, with a $3.50 hourly fee for usage in excess of five hours per month. Effective January 1, 1995 the hourly fee for usage in excess of five hours per month will decrease from $3.50 to $2.95.

The Company's marketing service revenues are generated from providing new media and interactive marketing services, including the aggregation and management of multimedia content databases, new media application development and outsourced marketing communications services.

The Company has received revenues from time to time in the form of funding ("other revenues") for certain product development activities conducted by the Company on behalf of

entities such as Apple Computer, Inc. (Apple). In December 1992 the Company entered into a seven year licensing and development agreement (with renewal provisions to extend the agreement through November 30, 2004) with Apple. Under the agreement, the Company granted Apple a non-exclusive license to use the America Online services platform to provide Apple-branded online services, and has agreed to provide development services to Apple on a fee for services basis. The Company will receive a royalty based on usage, with a total minimum royalty of $15 million over a five year period following the commercial launch of the Apple-branded online service. In addition to royalties, the Company received development funding leading up to the commercial launch of the Apple-branded online service. Apple commercially launched its branded online service, called eWorld, in June 1994. A total of approximately $4.6 million in development funding has been recognized to date under the Apple agreement. A total of $85,000 of development funding and $560,000 of royalty revenue has been recognized as "other revenues" in the three-month period ended September 30, 1994.

The competitive environment in the online services business continues to become increasingly more complex. The recent announcement by Microsoft Corporation of its online service is expected to impact the competitive environment.

Results of Operations

Revenues

For the three months ended September 30, 1994, total revenues increased from $19,079,000 to $54,423,000, or 185%, over the three months ended September 30, 1993. Online service revenues increased from $14,299,000 to $50,056,000, or 250%. This increase was primarily attributable to a 282% increase in revenues from IBM-compatible subscribers and a 222% increase in revenues from Macintosh subscribers as a result of a 226% increase in IBM-compatible subscribers and a 169% increase in Macintosh subscribers. The percentage increase in online service revenues for the three months ended September 30, 1994 was greater than the percentage increase in subscribers principally due to an increase in average monthly online service revenue per subscriber, which increased from $14.20 in the three months ended September 30, 1993 to $16.45 in the three months ended September 30, 1994. Marketing service revenues increased from $3,124,000 to $3,640,000, or 17%. Other revenues decreased from $1,656,000 to $727,000. This decrease was principally attributable to a decrease in Apple development revenues partially offset by Apple royalty revenues.

Cost of Revenues

Cost of revenues includes direct network-related costs, consisting primarily of data and voice communication costs, costs associated with operating the host computer system and providing customer support, royalties paid to information and service providers and production and other expenses related to marketing services. For the three months ended September 30, 1994 cost of revenues increased $11,165,000 to $31,955,000, or 186%, over the three months ended September 30, 1993, and increased as a percentage of total revenues from 58.5% to 58.7%.

The increase in cost of revenues was primarily attributable to an increase in data communication costs, customer support costs and royalties paid to information and service providers. Data communication costs increased primarily as a result of the larger customer base and more usage by customers. Customer support costs, which include personnel and

telephone costs associated with providing customer support, were higher as a result of the larger customer base and a large number of new subscriber registrations. Royalties paid to information and service providers increased as a result of a larger customer base and more usage and the Company adding more service content to broaden the appeal of the America Online service.

Marketing

Marketing expenses include the costs to acquire and retain subscribers and other general marketing expenses. For the three months ended September 30, 1994, marketing expenses increased from $3,719,000 to $11,295,000, or 204%, over the three months ended September 30, 1993, and increased as a percentage of total revenues from 19.5% to 20.8%. The increase in marketing expenses was primarily due to an increase in the number and size of marketing programs to expand the Company's subscriber base.

Product Development

Product development costs include research and development expenses, other product development costs and the amortization of software costs. For the three months ended September 30, 1994, product development costs increased from $1,040,000 to $1,757,000, or 69%, over the three months ended September 30, 1993, and decreased as a percentage of total revenues from 5.5% to 3.2%. The increase in product development costs was attributable to an increase in personnel costs related to an increase in the number of technical employees. The decrease in product development costs as a percentage of total revenues was a result of the substantial growth in revenues, which more than offset the additional product development costs. Product development costs, before capitalization and amortization, increased by 89% in the three months ended September 30, 1994.

General and Administrative

For the three months ended September 30, 1994, general and administrative expenses increased from $2,624,000 to $5,280,000, or 101%, over the three months ended September 30, 1993, and decreased as a percentage of total revenues from 13.8% to 9.7%. The increase in general and administrative costs was principally attributable to higher personnel, office and travel expenses related to an increase in the number of employees. The decrease in general and administrative costs as a percentage of total revenues was a result of the substantial growth in revenues combined with the semi-variable nature of many of the general and administrative costs.

Other Income

Other income consists primarily of rental and investment income net of interest expense. For the three months ended September 30, 1994, other income increased from $404,000 to $688,000, over the three months ended September 30, 1993. This increase was primarily attributable to an increase in interest income generated by higher levels of cash available for investment in the three months ended September 30, 1994, partially offset by a decrease in rental income received in the three months ended September 30, 1993.

Merger Expenses

Non-recurring merger expenses totaling $1,710,000 were recognized in the three months ended September 30, 1994 in connection with the merger of America Online, Inc. and Redgate Communications Corporation.

Income Taxes

Income tax expense was $1,315,000 and $1,848,000 in the three months ended September 30, 1993 and 1994, respectively.

Liquidity and Capital Resources

The Company has financed its operations through cash generated from operations, funding by third parties for certain product development and marketing activities, and sale of its common stock. Net cash provided by operating activities, including third-party development funding, was $5,603,000 and $18,969,000 in the three months ended September 30, 1993 and 1994, respectively. Net cash used in investing activities was $13,883,000 and $27,932,000 in the three months ended September 30, 1993 and 1994, respectively. These investing activities included investments in subscriber acquisition costs of $4,907,000 and $13,447,000 in the three months ended September 30, 1993 and 1994, respectively, as well as investments in property and equipment of $8,487,000, principally related to the purchase of the Company's office building, in the three months ended September 30, 1993.

In December 1993, the Company completed a public stock offering of 1,000,000 shares of common stock which generated net cash proceeds of approximately $62,700,000.

The Company uses its working capital to finance ongoing operations and to fund marketing programs and the development of its products and services. The Company plans to continue to invest aggressively in acquisition marketing programs to expand its subscriber base, as well as in computing and support infrastructure. Additionally, the Company expects to use a portion of its cash for the acquisition and subsequent funding of technologies, products and businesses complementary to the Company's current business. The Company anticipates that available cash and cash provided by operating activities will be sufficient to fund its operations for the foreseeable future.

The Company believes that inflation has not had a material effect on its results of operations.

PART II. OTHER INFORMATION

Item 6. Exhibits and Reports on Form 8-K

(a) Exhibits

None.

(b) Reports on Form 8-K

No reports on Form 8-K were filed during the quarter ended September 30, 1994.

AMERICA ONLINE, INC.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AMERICA ONLINE, INC.

DATE: November 14, 1994 SIGNATURE: ______________________

Stephen M. Case
Chief Executive Officer

DATE: November 14, 1994 SIGNATURE: ______________________

Lennert J. Leader
Chief Financial Officer
(Principal Financial Officer)